

NOV 27 1996

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NORTH CAROLINA
CHARLOTTE DIVISION

J. BARON GROSHON
BY: KLV
Deputy Clerk

In Re:) Case No. 95-31507
) Chapter 11
MIDDLE PLANTATION LIMITED PARTNERSHIP,)
)
Debtor.)

JUDGEMENT ENTERED ON NOV 27 1996

ORDER GRANTING MOTION FOR DISGORGEMENT OF RETAINER AND OTHER
FUNDS HELD BY DEBTOR'S COUNSEL

This matter is before the court on the Motion of Condor One, Inc., filed October 16, 1996 to disgorge certain funds held by the debtor's counsel. After considering the Motion for Disgorgement, the debtor's Response to Motion and Motion to allow further fees, and the arguments made during the November 13, 1996 hearing on these motions, it is this court's finding that the Motion for Disgorgement should be granted and that no attorney fees should be allowed from the \$10,000 retainer held by debtor's counsel, the \$2,643.52 NationsBank account, or any other funds presently in the debtor's possession.

An Order Denying Application for Interim Attorney Fees was entered by this court on April 23, 1996 after debtor's attorney requested compensation drawn against the \$10,000 retainer for expenses of \$643.44 and for services in the amount of \$7,682.50.

(82)

This order incorporates the prior Order's Findings of Fact and Conclusions of Law as they still reflect accurately the views of this court in this matter. However, further findings are relevant to the disgorgement and denial of all debtor's attorney fees.

Findings of Fact

1. Condor One, Inc. is the sole secured creditor of the debtor in what is accurately characterized as a "single asset," "two party" case. The single asset is a 124-unit apartment complex commonly known as Middle Plantation Apartments ("the property").

2. Condor One is an undersecured creditor. The property has been appraised and has an estimated value of \$2.5 million, while Condor One holds the Deed of Trust Note in the original principal amount of \$3.15 million and the Deed of Trust and Assignment of Rents, Profits and Income, both dated April 29, 1986. The debtor has no source of income or revenue other than the rents, issues and profits generated from the property.

3. On or about September 26, 1995, a \$10,000 retainer fee was paid to the law firm of Rayburn, Moon & Smith, P.A. for legal services (see Rule 2004 examination testimony of Tom G. Thornburg attached to Condor's Motion for Disgorgement).

4. By letter dated September 28, 1995, Condor One notified the debtor of defaults existing under the Note and the Deed of Trust.

5. This case was commenced by the filing of an involuntary petition against the debtor on October 11, 1995 under Chapter 11 of the Bankruptcy Code.

6. R. Keith Johnson entered a Notice of Appearance as attorney for the debtor on December 6, 1995.

7. Johnson filed a request for interim attorney fees and expenses on March 8, 1996 to which Condor One objected and which was denied in a judgment entered April 23, 1996.

8. The debtor has failed to confirm its plan of reorganization and Condor One has been granted relief from the stay.

Conclusions of Law

1. All rents, issues and profits arising from the property prior to the entry of the order for relief are either the property of Condor One or its cash collateral, because Condor One is the current holder of the Deed of Trust Note and the Deed of Trust and Assignment of Rents, Profits and Income, the debtor was given notice of the default on the Note and Deed of Trust, and an order for relief was entered by this court.

2. Section 330 of the Bankruptcy Code allows a debtor's attorney to apply for reasonable compensation for services and expenses, which must be approved by the bankruptcy court. The general rule, however, is that administrative expenses occurring post-petition are not permitted to be charged against secured collateral where the creditor is neither oversecured nor adequately protected. *In re Visual Industries, Inc.*, 57 F.3d 321, 324 (3d Cir. 1995). In other words, administrative fees, such as attorney fees and expenses, are the responsibility of the debtor's estate -- not the secured creditors'. The exception to this rule is found in 11 U.S.C. § 506(c), which allows certain reasonable, necessary costs and expenses which are necessary to preserve or dispose of the property to be charged against the secured creditors' collateral to the extent of any benefit to the holder of such secured claim. While secured creditors are not liable for administrative expenses, they are liable for expenses related to maintaining their collateral's value or for its liquidation.

2. As outlined in this court's previous Order, there are two tests for determining which claims for reimbursement are recoverable: an objective and a subjective test. The subjective test considers whether the secured creditor expressly requested or consented to the expenditures. There has been no evidence

presented from which this court could find such consent. The fact that Condor One objected to the interim fees would be evidence to the contrary.

The objective test has three prongs. The charges must be (1) necessary to preserve or dispose of the property, (2) of benefit to the secured creditor, and (3) reasonable. The burden of proof as to these factors is on the professional requesting the fees. This burden has not been met.

To satisfy the benefits prong the claimant must establish in quantifiable terms that it expended funds directly to protect and preserve the collateral. *In re Flagstaff Foodservice Corp.*, 762 F.2d 10, 12 (2d Cir. 1985), *In re Visual Industries, Inc.*, 57 F.3d 321, 324 (3d Cir. 1995). Incidental, indirect, or secondary benefits to the creditor will not suffice in the objective test. *In re Mall at One Associates*, 185 B.R. 981 (E.D.Pa. 1995), *In re Flagstaff Foodservice Corp.*, 739 F.2d 73 (2d Cir. 1984).

Here, any compensation paid to the debtor's attorney would be paid from the secured creditor's collateral. There is no other source of income to the debtor and there are no unencumbered assets. Condor One is undersecured, so there is no equity in this property that might be usable under 11 U.S.C. §363 (subject to adequate protection). The sole avenue to the use of the collateral

by the debtor in this case would be under 11 U.S.C. § 506, which is not available because the debtor's use does not meet the three-prong test already discussed. Because Condor One is the sole secured creditor, there is no dispute as to what creditor has rights in these funds, which means that this bankruptcy filing did not aid Condor One, directly or indirectly, or preserve the collateral for Condor One's benefit. On the contrary, it has slowed their debt collection. Attorney's fees incurred primarily to assist the debtor in the reorganization process are not generally chargeable against secured collateral where the creditor is undersecured and not adequately protected. Thus, there has been no benefit to the secured creditor. Condor One's collateral is being used to fight Condor One.

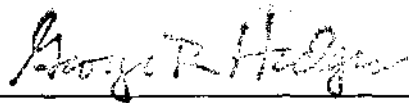
Neither has there been any showing that the attorney's services were necessary for the preservation of the property.

3. Although part of the money at issue, the \$10,000 retainer, was paid prior to the Notice of Default to the Debtor, these funds are still subject to the court's powers to order disgorgement under 11 U.S.C. § 330. While the money's status as a retainer created a security interest in the funds, it does not render them immune from this provision. At the time the Notice of Default was sent, Keith Johnson had not yet been employed by the

debtor and none of the retainer had been used, so all the funds became subject to this court's review.

It is therefore **ORDERED** that the Motion for Disgorgement of Retainer and Other Funds held by Debtor's Counsel submitted by Condor One is **Granted**.

Dated: November 27, 1996.



George R. Hodges
United States Bankruptcy Judge